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**GARISSA UNIVERSITY**

**UNIVERSITY EXAMINATION 2017/2018 ACADEMIC YEAR ONE**

**THIRD SEMESTER EXAMINATION**

**SCHOOL OF BUSINESS AND ECONOMICS**

**FOR THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION**

**COURSE CODE: MBA 811**

**COURSE TITLE: FINANCIAL MANAGEMENT**

**EXAMINATION DURATION: 2 HOURS**

**DATE: 06/08/18 TIME: 09.00-12.00 PM**

**INSTRUCTION TO CANDIDATES**

* **The examination has SIX (6) questions**
* **Question ONE (1) is COMPULSORY**
* **Choose any other THREE (3) questions from the remaining FIVE (5) questions**
* **Use sketch diagrams to illustrate your answer whenever necessary**
* **Do not carry mobile phones or any other written materials in examination room**
* **Do not write on this paper**

**This paper consists of FOUR (4) printed pages *please turn over***

**QUESTION ONE (COMPULSORY)**

1. Giving examples of each and the tools and models required, explain four critical decisions made by finance managers of business organizations **[7 marks]**
2. Roberts Ltd.’s dividend per share is expected to be Shs. 4, and it is expected to grow at a 6 percent rate forever. The company also has a 9 percent, Shs. 1,000 -par-value preferred stock issue. According to the company, the appropriate discount rate is 14 percent. Determine the value of a common stock share and a preferred stock share of Roberts Ltd **[2 marks]**
3. Differentiate the following terms as used financial management
4. Systematic risk and unsystematic risk **[2 marks]**
5. Capital Asset Pricing Model (CAPM) and Arbitrage Pricing Theory (APT) **[2 marks]**
6. Capital Market Line (CML) and Security Market Line (SML) **[2 marks]**

**QUESTION TWO**

1. Explain why NPV is a preferred technique of project evaluation over the other techniques

**[5 marks]**

1. Karata ltd has two projects with the following annual cash flows.

Project 1 Project 2

Years KshKsh

0 1,000,000 1,000,000

1 250,000 300,000

2 250,000 200,000

3 250,000 300,000

4 250,000 400,000

5 250,000 150,000

Given that, the discount rate for the company is 10%,

**Required:**

1. Compute the NPV of the projects and advice **[5 marks]**
2. Determine the IRR of the project as per your advice in (i) above **[5 marks]**

**QUESTION THREE**

1. Briefly explain the concept‘optimal capital structure’ and its determinants **[5 marks]**
2. Discuss any two capital structure theories that you know, state the assumptions and the application of each to the current corporate world. **[10 marks]**

**QUESTION FOUR**

1. Identify and explain three types of dividends **[3 marks]**
2. Clearly explain the factors that influence dividend policy using local examples from Kenyan companies **[6 marks]**
3. Kasuku Ltd has a dividend payout policy of 45% and its EPS is sh. 50.20. The rate of return on internal funds is 16%. The owners require a capitalization rate of 12%.

**Required:**

Determine the current market value per share using the two models and advise accordingly

1. Gordon model
2. Walter model **[6 marks]**

**QUESTION FIVE**

Mazao Co. Ltd. had the following capital structure as at 31 December 2017:

|  |  |
| --- | --- |
|  | **Shs**. |
| Ordinary share capital (600,000 shares) | 6,000,000 |
| 14% Preference share capital | 2,000,000 |
| 10% Debenture capital | 4,000,000 |
|  | 10,000,000 |

**Additional information:**

1. The market price of each ordinary share as at 31 December 2017 was Shs. 32.
2. The company paid a dividend of Shs. 2.98 for each ordinary share for the year ended 31 December 2016.
3. The annual growth rate on the earnings and dividends was estimated at 8%.
4. The corporation tax rate is 40%.

**Required:**

1. Compute the weighted average cost of capital of the company as at 31 December 2017 **[9 marks]**
2. Explain the two main assumptions and two applications of WACC **[6 marks]**

**QUESTION SIX**

1. Explain three main determinants of working capital management **[3 marks]**
2. Briefly, explain TWO risks of holding more cash balances and TWO motives for holding cash by a firm **[4 marks]**
3. Discuss the importance of financial ratios in planning for working capital  **[8 marks]**